ORIGINAL

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS
GARY PIERCE - Chairman
BOB STUMP
SANDRA D. KENNEDY
PAUL NEWMAN
BRENDA BURNS

IN THE MATTER OF THE APPLICATION OF ARIZONA WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR ADJUSTMENTS TO ITS RATES AND CHARGES FOR UTILITY SERVICE FURNISHED BY ITS EASTERN GROUP AND FOR CERTAIN RELATED APPROVALS.	DOCKET NO. W-01445A-11-0310 **STAFF'S NOTICE OF FILING WITNESS SUMMARIES**

The Utilities Division ("Staff") of the Arizona Corporation Commission ("Commission") hereby files the testimony summaries of Staff witnesses Katrin Stukov, Jeffrey M. Michlik, John A. Cassidy and D. Bentley Erdwurm in the above-referenced matter.

RESPECTFULLY SUBMITTED this 11th day of May, 2012.

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SUMMARY OF TESTIMONY OF
KATRIN STUKOV
ARIZONA WATER COMPANY
DOCKET NO. W-01445A-11-0310

My Direct Testimony provides the Utilities Division Staff's ("Staff") engineering evaluation of Arizona Water Company's ("AWC" or "Company") water systems for this rate case proceeding. Exhibit KS to my Direct Testimony presents AWC water systems' details and Staff's analysis and findings. This report contains the following major topics: (1) a description and analysis of each water system, (2) water use, (3) growth, (4) compliance with the rules of the Arizona Department of Environmental Quality and Arizona Department of Water Resources, and (5) depreciation rates.

Staff recommends:

- an annual water testing expense of $43, 843 for this proceeding (which excludes the ADEQ Monitoring Assistance Program expense of $33,764).

- the continued use of the previously approved depreciation rates developed by the Company.

- the acceptance of the Company's requested service line and meter installation charges.

- that if any of the Company's water systems should be consolidated for purpose of rate making and accounting, AWC be required to continue reporting information such as, but not limited to, Water Use, Water Loss and Plant Description Data, separately for each of its individual systems by Public Water System, as defined by ADEQ, in future Annual Reports and rate filings.

- adoption of the Off-site Facilities Fee Tariff discussed in Section VIII and shown in Attachment A. Staff recommends that the Company submit a calendar year Off-Site Facilities Fee status report each January to Docket Control for the prior calendar year, beginning January 2013, until the hook-up fee tariff is no longer in effect. This status report shall contain a list of all customers that have paid the hook-up fee tariff, the amount each has paid, the amount of money spent from the tariff account, the amount of interest earned on the tariff account, and a list of all facilities that have been installed with the tariff funds during the 12 month period.

- That the Company continue to record and monitor monthly water losses, repair any leak as soon as it is discovered and implement an aging infrastructure replacement as discussed in the report.

SUMMARY OF SURREBUTTAL TESTIMONY OF KATRIN STUKOV

The purpose of my Surrebuttal Testimony is to respond to the Company's Rebuttal Testimony of Fredrick Schneider, specifically relative to the statement that Staff has offered no evidence that the Company's proposed amount of $3,500 Off-Site Facilities Fee is not reasonable.

SUMMARY OF TESTIMONY OF
JEFFREY M. MICHLIK
ARIZONA WATER COMPANY
DOCKET NO. W-01445A-11-0310

The testimony of Mr. Michlik addresses the following outstanding issues:

Rate Base Issues

Plant Not Used – The Company proposes to include in rate base plant items that were not used and useful in the test year but were placed back into service more than a year after the test year. It is inappropriate to reach more than a year beyond the test year to include plant in rate base simply because it was previously in service.

Cash Working Capital – Staff continues to recommend excluding of the Company's proposed equity component from the lead/lag study.

Income Statement Issues

Fleet Fuel Expenses – Due to the price volatility of gasoline, Staff recommends using a 12-month historic average price of gasoline in Arizona for determining the fuel cost.

Removal of Projected Transmission and Distribution Expenses – Staff continues to recommend removal of projected transmission and distribution expenses. The projections are not known and measurable and, even if such projections were appropriate, the Company's regression analysis is fraught with faults and is statistically invalid.

Rate Case Expense – Staff continues to recommend a reasonable rate case expense based on reasonable cost efficiencies the Company should have taken when it filed its rate cases.

Amortization of a prior deferred regulatory asset – Staff continues to recommend the yearly amortization amount that the Commission established in a prior rate case.

Alternative to DSIC

Staff recommends denial of a DSIC. Instead, Staff proposes a "Sustainable Water Loss Improvement Program" for the Miami and Bisbee systems, consisting of deferred depreciation and return for up to 24 months after in-service date for certain limited projects. If the Commission adopts a DSIC, Staff recommends that it include the requirements set forth in Staff's surrebuttal testimony.

SUMMARY OF TESTIMONY OF
JOHN A. CASSIDY
ARIZONA WATER COMPANY
DOCKET NO. W-01445A-11-0310

The following is a summary of the Surrebuttal testimony of Staff witness John A. Cassidy:

Capital Structure – Staff continues to recommend that the Commission adopt a capital structure for Arizona Water Company ("Company") for this proceeding consisting of 49.0 percent debt and 51.0 percent equity.

Cost of Equity – Staff recommends that the Commission adopt a 9.4 percent return on equity ("ROE") for the Company. Staff's estimated ROE for the Company is based on the average of its DCF and CAPM cost of equity methodology estimates for the sample companies ranging from 9.0 percent for the discounted cash flow method ("DCF") to 9.7 percent for the capital asset pricing model ("CAPM").

Overall Rate of Return – Staff recommends that the Commission adopt an 8.1 percent overall rate of return.

Dr. Zepp's Testimony – The Commission should reject the Company's proposed 12.50 percent ROE for the following reasons:

> Dr. Zepp's primary and secondary DCF models use average stock prices to calculate the current dividend yield, his primary DCF estimates rely exclusively on analysts' forecasts for earnings per share growth, his secondary DCF estimates fail to consider historical dividend per share growth and are based, in part, on historical average share price appreciation. Dr. Zepp's CAPM and risk premium estimates utilize a forecasted risk-free rate.

Ms. Ahern's Rebuttal Testimony – The Commission should reject the Company's proposed 12.50 percent ROE for the following reasons:

> Ms. Ahern's testimony contravenes the metrics used by Dr. Zepp and implies that his estimate of the Company's cost of equity is overstated by 159 basis points.

SUMMARY OF TESTIMONY OF
D. BENTLEY ERDWURM
ARIZONA WATER COMPANY
DOCKET NO. W-01445A-11-0310

This testimony includes Staff recommendations related to rate design and a normalization adjustment proposed by the Company related to use-per-customer. Staff's rate design recommendations conform to the revenue requirement recommendations of Staff witness Mr. Jeffery Michlik and generally include an inclining block structure (with the exception of a flat structure for larger industrial customers (meters >=6 inches) and sales for resale). Under the inclining block structure, volumetric (usage) rates (per gallon) increase as usage increases. The structure promotes the efficient use of scarce water resources. To provide additional options for the Commission, Staff proposes two sets of rate alternatives for consideration. Alternative 1 most closely follows the design approach presented by Staff in Direct Testimony. Alternative 2 has higher customer charges than Alternative 1. Both alternatives make residential basic needs service available for a nominal charge and both designs promote the efficient use of scarce resources.

Staff is not supporting full consolidation of rates over the entire Eastern system at this time. Moving to consolidated rates would create large bill increases for larger customers on systems that have lower than average rates. Apache Junction, Superior, and Miami are presently consolidated for ratemaking purposes (as "Superstition"), and this consolidation was maintained in Staff's Direct and Surrebuttal rate recommendations. Staff previously has reviewed the possibility of consolidating Bisbee and Sierra Vista under uniform "Cochise" rates; however, customer impacts on Sierra Vista customers would have been too great. Bisbee and Sierra Vista presently have the same customer charge, a feature that was maintained in the Staff Direct and Surrebuttal recommendations. Staff is not consolidating San Manuel, Oracle and SaddleBrook Ranch at this time because of the significant adverse impact on San Manuel customers. However, Oracle and SaddleBrook Ranch are partially consolidated under the Staff recommendation (volumetric charges are equal under Staff's Alternative 1 recommendation). Winkleman remains a stand-alone system.

Staff in Surrebuttal Testimony modifies its position on the Company's proposed commercial use-per-customer adjustments applicable to the Superstition service area. In Direct testimony Staff recommended the rejection of all use-per-customer normalization adjustments because the Company's change in use-per-customer estimates – the basis for the normalization adjustments – typically are statistically unstable and vary with the time frame of the analysis (e.g. 10 year vs. 5 year). However, Staff acknowledges that when the adjustments are evaluated on a case-by-case basis, the Superstition-Commercial estimates are robust (consistent under different model formulations) and statistically significant. While Staff acknowledges the appropriateness of some use-per-customer adjustment for the Superstition service area, Staff proposes a scaling-back of the Company's proposed commercial adjustment for Superstition.